

Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:CORP:01

PLR-107892-09

Date:

June 04, 2009

Legend

Distributing =

Controlled =

State X =

Date 1 =

Date 2 =

Group A Shareholders =

Group B Shareholders =

X =

Y =

Business 1 =

Dear :

This letter responds to your representative's letter dated December 1, 2008, requesting rulings as to the Federal income tax consequences of a proposed transaction. Additional information was submitted by letters dated April 17, 2009, May 11, 2009, and June 1, 2009. The material information submitted for consideration is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process. In particular, this office has not reviewed any information pertaining to, and has made no determination regarding, whether the proposed transaction: (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code (the "Code") and § 1.355-2(d)); or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest in the distributing corporation or the controlled corporation (see § 355(e) and § 1.355-7).

SUMMARY OF FACTS

Distributing was organized as a subchapter C corporation, in State X, on Date 1. Effective Date 2, Distributing elected to become an S corporation. Distributing is owned by two shareholder groups. The Group A Shareholders together own X% and the Group B Shareholders together own Y% of the stock of Distributing.

Distributing is engaged in Business 1. Distributing has submitted financial information which indicates that Business 1 has had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

PROPOSED TRANSACTION

For what are represented as valid business reasons, Distributing proposes the following transactions (the “Proposed Transaction”):

- (i) Controlled will be incorporated in State X. Controlled will have one class of common stock outstanding, all of which will be owned by Distributing.
- (ii) Distributing will transfer assets and liabilities related to the conduct of Business 1 to Controlled in exchange for all of the Controlled stock (the “Contribution”).
- (iii) Immediately after the Contribution, Distributing will distribute all of the Controlled stock to the Group B Shareholders in exchange for all of their Distributing stock (the “Distribution”). Thereafter, the Group A Shareholders will own all of the Distributing stock and the Group B Shareholders will own all of the Controlled stock.

REPRESENTATIONS

The taxpayer has made the following representations concerning the Proposed Transaction:

- (a) The fair market value of the Controlled stock to be received by the Group B Shareholders will be approximately equal to the fair market value of the Distributing stock surrendered by the Group B Shareholders in the exchange.
- (b) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee or in any capacity other than that of a Distributing shareholder.
- (c) The five years of financial information submitted on behalf of Distributing, concerning Business 1, represents its present operations, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (d) The five years of financial information submitted on behalf of the business contributed to Controlled is representative of the business’s present operation, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (e) Following the transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees.
- (f) Neither Business 1 nor control of an entity conducting this business will have been acquired during the five-year period ending on the date of the Distribution in

a transaction in which gain or loss was recognized (or treated as recognized) in whole or in part.

- (g) The Distribution is carried out for the following corporate business purposes: to resolve deadlock among the management of Distributing which threatens the continued operation of its business and exposes it to the risk of lost profits, foreclosure, the loss of customers and various other severe financial consequences. The distribution of the stock, or stock and securities, of Controlled is motivated, in whole or substantial part, by this corporate business purpose.
- (h) The transaction is not used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.
- (i) The total adjusted bases of the assets to be transferred to Controlled by Distributing in the transaction will equal or exceed the sum of the total liabilities assumed (within the meaning of section 357(d)) by Controlled.
- (j) The liabilities assumed (within the meaning of § 357(d)) by the controlled corporation in the contribution were incurred in the ordinary course of business and are associated with the assets being transferred.
- (k) The total fair market value of the assets transferred to Controlled in the transaction will exceed the sum of (i) the amount of any liabilities assumed (within the meaning of section 357(d)) Controlled in the exchange, and (ii) the amount of any liabilities owed to Controlled by Distributing that are discharged or extinguished in connection with the exchange. The fair market value of the assets of Controlled will exceed the amount of its liabilities immediately after the exchange.
- (l) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- (m) No income items, including accounts receivable or any item resulting from a sale, exchange or disposition of property, that would have resulted in income to the distributing corporation, and no items of expense will be transferred to the controlled corporation if the distributing corporation has earned the right to receive the income or could claim a deduction for the expense under the accrual or similar method of accounting.
- (n) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to the Distribution.

- (o) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.
- (p) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution, or (ii) attributable to distributions on Distributing stock or securities that were acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.
- (q) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (r) No two parties to the transaction are investment companies as defined in §§ 368(a)(2)(F)(iii) and (iv).
- (s) The Distribution is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).
- (t) Immediately after the transaction (as defined in § 355(g)(4)), neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of § 355(g)(2)).
- (u) Effective Date 2, Distributing made an election under § 1362(a) to be an S corporation (within the meaning of § 1361(a)), and Distributing has continued to be an S corporation since Date 2 (within the meaning of § 1361(a)).
- (v) Immediately after the transaction, Controlled will be eligible to elect S corporation status pursuant to § 1362(a), effective immediately after the transaction.

- (w) Controlled will elect to be treated as an S corporation, effective immediately after the Distribution (see § 1.1361-3(a)(4)).
- (x) None of the persons holding stock, membership interests, or any equity interest in either Distributing or Controlled is a nonresident alien individual, a foreign corporation, or a trust (except for trusts meeting the requirements of Section 1361(c)(2)).
- (y) There is no plan or intention to revoke or otherwise terminate the S corporation election of either Distributing or Controlled.

RULINGS

Based solely on information submitted and the representations set forth above, we rule as follows:

- (1) The Contribution, followed by the Distribution will constitute a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled each will be “a party to a reorganization” within the meaning of § 368(b).
- (2) No gain or loss will be recognized by Distributing upon the Contribution. Sections 361(a) and 357(a).
- (3) No gain or loss will be recognized by Controlled on the Contribution. Section 1032(a).
- (4) The basis of each asset received by Controlled in the Contribution will equal the basis of that asset in the hands of Distributing immediately prior to its transfer. Section 362(b).
- (5) The holding period for each asset received by Controlled from Distributing will include the period during which Distributing held the asset. Section 1223(2).
- (6) No gain or loss will be recognized by Distributing on the Distribution. Section 361(c).
- (7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) the Group B Shareholders upon their receipt of Controlled stock in exchange for their Distributing stock. Section 355(a).
- (8) The basis of the Controlled stock in the hands of the Group B Shareholders after the Distribution will, in each instance, equal the basis of the respective Distributive stock surrendered by the shareholder in exchange therefore. Section 358(a)(1).

- (9) The holding period of the Controlled stock received by Group B Shareholders will, in each instance, include the holding period of the Distributing stock held by each respective shareholder, provided that each respective shareholder held the Distributing stock as a capital asset on the date of the Distribution. Section 1223(1).
- (10) Proper allocation of Distributing's earnings and profits will be made under Sections 312(h) and 1.312-10(a).
- (11) Controlled will be subject to § 1374 with respect to any asset transferred in the Contribution to the same extent that Distributing is subject to § 1374 with respect to such asset. For purposes of § 1374, Controlled's recognition period will be reduced by the portion of Distributing's recognition period that expires prior to the Contribution (§ 1374(d)(8) and Ann. 86-128, 1986-51 I.R.B. 22).
- (12) Distributing's momentary ownership of the stock of Controlled, as part of the reorganization under § 368(a)(1)(D), will not cause Controlled to have an ineligible shareholder for any portion of its first taxable year under § 1361(b)(1)(B). If Controlled otherwise meets the requirements of a small business corporation under § 1361, Controlled will be eligible to elect to be a subchapter S corporation under § 1362(a) for its first taxable year.

CAVEATS

No opinion is expressed about the tax treatment of the Proposed Transaction described above under other provisions of the Code and regulations or the tax treatment of any condition existing at the time of, or effects resulting from, the Proposed Transaction that is not specifically covered by the above rulings. In particular, no opinion is expressed regarding: (i) whether the Proposed Transaction satisfies the business purpose requirement of § 1.355-2(b); (ii) whether the Proposed Transaction is used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both (see § 355(a)(1)(B) and § 1.355-2(d)); and (iii) whether the Proposed Transaction is part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii).

PROCEDURAL STATEMENTS

This ruling letter is directed only to the taxpayer who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

In accordance with the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Lisa A. Fuller
Senior Counsel, Branch 1
Office of Associate Chief Counsel (Corporate)